

### **III.B.1.a**

MEMO TO: City Council

FROM: Lenda Crawford, Finance Director

DATE: July 15, 2003

SUBJECT: **STAFF REPORT: Financial Status Report for 1<sup>st</sup> Quarter 2003**

City financial policies require periodic financial reports that summarize activity by major fund type. Accordingly, this report summarizes the financial performance of the major city funds, including the General, Capital and Enterprise funds for the first three months of the 2003 – 2004 biennium.

Staff will be present at the July 15 Council meeting to answer any questions on the report. If you have questions prior to that time, please contact either Lenda Crawford at 425.556.2160 or Martin Chaw at 425.556.2165.

## EXECUTIVE SUMMARY

While the greater Puget Sound area continues to suffer from the effects of a weak economy, the City of Redmond is faring relatively well. The City's General Fund, Utilities and Capital Investment Program (CIP) continue to operate within budget. In addition, sales tax revenue, which is the city's largest revenue source and highly sensitive to changes in the economy, has begun to stabilize as a result of several new retailers (Home Depot, Fred Meyer, Cost Plus Imports) coming to town. This revenue source should get a further boost later in the year with the opening of the Bon Marche and Staples Office Supply, followed by the opening of a full service Marriott Hotel in 2004. Also, the City's major employer, Microsoft, continues to hire and is nearing completion of its newest five story 325,000 square feet building.

Although the general outlook for the City is positive, the recovery at the national and regional levels continues to pose a risk. The general US economy, as measured by the Gross Domestic Product (GDP), has grown consistently since the last quarter of 2001 and, most recently, grew by 1.9% during the 1<sup>st</sup> quarter of 2003. However, this is significantly slower than years past when the economy grew between 4% to 5% annually. Additionally, significant weakness in the nation's labor market continues to weigh upon the economic recovery. Nationally, the unemployment rate has risen to 6.1%. This compares to the state's unemployment rate of 7.3%, which is one of the highest in the nation. The local unemployment rate stands at 6.6% for King County.

The weakness in the national economy, continues to be mitigated by consumer spending, which fuels about two thirds of the nation's growth. The index of Consumer Confidence, which is a proxy for consumer spending, increased in April reflecting the conclusion of the Iraq War. While consumers continue to express concern over the nation's unemployment rate, this concern does not appear to be having a significant impact on their spending habits. This is because consumer spending is primarily being fueled by lower interest rates. These rates are expected to remain low in the foreseeable future or until such time the Federal Reserve is convinced that the recovery is well underway.

While economic conditions remain tenuous, the recent improvements in GDP and consumer confidence are causing some economists to begin to modify their forecasts and predict a national recovery as early as late 2003 or early 2004. The Puget Sound area is expected to lag national trends by six to nine months.

### **General Fund**

As of the end of the first quarter, General Fund operations are in line with expectations. Revenues are on target with the exception of development fees, which continue to remain at low levels mirroring ongoing weakness in commercial construction. Expenditures are running approximately 2% below budget at this point as the city continues to scrutinize its expenses closely and remains cautious about the economic recovery. It is important to note that since this is only the first quarter of the biennium, it is too early to draw any meaningful conclusions from this data. It will be necessary to monitor both revenues and expenditures closely over the next several months for any significant changes in trends to get a better picture of the course of the recovery and its effects upon city operations.

**Revenues:** General fund revenues totaled \$13.8 million compared to \$9.5 million for the same period last year. Highlights of first quarter revenue performance include:

- **Beginning fund balance.** The General Fund started the biennium with \$5.0 million. This balance includes \$3.3 million in funds that were carried forward from 1999-2000 and is presently being reserved in the event economic conditions worsens. The remaining

\$1.7 million represents funding that was set-aside in 2001-2002 for labor contracts that have not yet been settled and will be carried forward to 2003 for the same purpose.

- **Sales taxes** have begun to stabilize with a stronger than expected performance in retail sales. First quarter collections totaled \$3.4 million compared to \$3.5 million for the same period last year. Sales from retailers grew by 7% over 2002 and were led by the opening of Home Depot. Fred Meyer also had a positive impact on the City's retail sales, growing the general merchandise segment by 8.5%. Offsetting most of these increases were declines in sales taxes from construction associated with commercial development.

The following chart compares Redmond's retail sales activity with surrounding jurisdictions.

**% Change in Sales Tax Collections: 1Q 2002 v 1Q 2003**

Seattle	-4.3%
Unincorporated King Co.	-2.3%
Bothell	-2.0%
Redmond	-2.0%
Bellevue	-1.8%
Renton	-.6%
Tukwila	.7%
Kirkland	3.0%

- **Property tax** collections are in-line with expectations. The majority of the City's property taxes are collected two times during the year, May/June for the April property tax bill payments and November/December for the October payments.
- **Utility taxes** were \$2.1 million or 11% collected and is consistent with expectations for this time of year.
- **Development revenues** continue to be weak as stated earlier, with collections of \$753,000 compared to \$1.4 million for the same period last year.
- **Intergovernmental revenues** are lower than last year. However, this is a timing issue related to the receipt of payment for fire protection services. Payments from Fire District 34 occur twice a year in July and December.
- **Other revenues** totaled \$1.6 million compared to \$1.4 million the previous year. The increase primarily reflects stronger than anticipated business license revenues. This revenue source is up \$500,000 due to enhanced auditing efforts. Offsetting a portion of this increase is a decline in interest earnings. Interest revenues are lower due to the overall decline in interest rates as well as a decline in cash balances for the General Fund.

**Expenditures:** General fund departments ended the first quarter with expenditures totaling \$11.2 million or 10.8% of budget. This represents approximately a 1.7% savings rate when compared to the first quarter benchmark of 12.5% of the biennial budget. The city has incurred savings primarily in the salaries and benefits areas as a result of continuing to scrutinize vacant positions and hiring only after a business case has been made. Additionally, the Fire Department continues to work with its Union in managing its overtime costs and has reduced this expense by \$25,000 in the first quarter.

Please refer to the attached appendix for further detail on General Fund revenues and expenditures by department.

### **Enterprise Funds**

The **Water/Wastewater Utility** operating condition continues to improve in comparison to prior years. The Utility first quarter loss narrowed to \$50,000 from \$400,000 for the same period in 2002. First quarter operations have improved as a result of a 10% increase in water consumption and higher rates that went into affect January 1, 2003. Traditionally, an operating loss occurs during the first quarter of each year, reflecting relatively lower water consumption during the cooler months. This loss is typically made up during the summer when the Utility experiences a relatively higher volume of water sales.

Expenses for the **Water/Wastewater Utility Construction Fund** during the first three months totaled \$493,000. Current period expenditures reflect the reconstruction of well number 5. Design for this project is underway with construction expected in early 2004.

The **Stormwater Management Utility** ended the first quarter on a positive note with net operating income of \$175,000 compared to \$283,000 for the same period last year. Operating income decreased as a result of higher salary costs related to the filling of vacancies in the maintenance and operations section as well as increased water quality monitoring fees payable to King County for the Bear Creek rehabilitation project. Both of these events were anticipated in the budget.

Expenses for the **Stormwater Management Construction Fund** totaled \$177,000. The majority of these expenditures was for the rehabilitation of Idylwood Stream, which is nearly complete. Other significant projects worked on during the first quarter include construction design for both the Welcome Park retention pond and the third phase of rehabilitation of Upper Peters Creek. Both projects are scheduled for construction in summer 2003.

The **Urban Planned Development Utility** financial position is also improving. The Utility incurred a net operating loss of \$139,000 for the first quarter compared to a loss of \$275,000 during the same period 2002. The improvement is the result of an increase in rate revenues. Although rate revenues continue to increase, expenses including depreciation are still higher than revenues. Staff expects this to correct itself over time as revenue received from the depreciation rate surcharge are collected and recognized as income.

No major expenses were reported for the **Urban Planned Development Construction Fund**.

### **Capital Construction Funds**

CIP revenues continue to be sufficient to finance the City's construction program. Historically, expenditures for the City's CIP program are relatively low during the first quarter as the construction season has not fully started and pick up between spring and fall. Expenses for the first quarter of this biennium are consistent with historical trends.

**Overall, CIP revenues** are on target at the end of the first quarter. Revenues total \$7.5 million and are fairly consistent with last year. Business tax and impact fee revenues are running ahead of budget at this point, while vehicle registration fees and interest earnings are coming in below budget. Following is a summary of performance by major revenue categories.

- **Real estate excise taxes** are flat with collections totaling \$525,000 compared to \$575,000 for the same period last year. Sales of moderately priced homes continue to be in high demand, offsetting the decline in large commercial sales.
- As stated earlier, **business tax revenues** are higher than expected. Collections totaled \$3.9 million compared to \$3.1 million collected for the same period last year. The increase in collections is attributable to enhanced auditing efforts for this activity.

- **Impact fee revenues** are up in comparison to last year. The City has collected \$1.2 million compared to \$556,000 for the same period last year. Impact fees can vary significantly as these revenues are deposited into the CIP upon completion of projects.
- **Vehicle registration fees** are down as expected due to the elimination of the \$15 local option vehicle license fee as approved by voters in Initiative 776. The \$10,000 received to date represents fees paid last year but were not distributed by the State to the City until January.
- **Interest earnings** are coming in lower than expected primarily due to the rapid decline in interest rates and its corresponding effects on the city's investment portfolio.

**CIP expenses** totaled \$1.4 million compared to \$3.4 million for the same period last year. In 2002, expenses were higher during the first quarter due to the construction of the West Lake Sammamish Parkway project (WLSP) from Marymoor to Leary Way. While other CIP projects are underway in the city, the timing of these expenditures will vary widely from year-to-year. The following provides a brief recap of CIP activities by functional area.

- **Fire functional area expenditures** are essentially unchanged relative to last year and reflect only transfers to the Fire Equipment Replacement fund.
- **Transportation functional area expenditures** totaled \$1.0 million compared to \$2.7 million the same period last year. As mentioned earlier, expenses were high in 2002 due to the construction of the WLSP. Expenditures this quarter reflect activities for a multitude of projects including Redmond Way/132<sup>nd</sup> Ave NE right turn lane construction, 148<sup>th</sup> Ave NE/NE 40<sup>th</sup> Street improvements, and 166<sup>th</sup> Avenue NE improvements. Other significant projects include award of bid for WLSP Rehabilitation from Bellevue Redmond Road to NE 24<sup>th</sup> Street and for WLSP from Marymoor to NE 51<sup>st</sup> Street.

On a related matter, a statewide **transportation package** valued at \$4.2 billion over 10 years was recently approved by the Legislature. To finance the package, the gasoline tax is increased by 5 cents per gallon, trucking fees by 15% and a .03 percent sales tax surcharge is added on new and used vehicles. These tax and fee increases are effective July 1, 2003. Projects in this package affecting **Redmond** include: \$102 million to extend **carpool lanes** on SR520 from West Lake Sammamish Parkway to SR202; \$11.2 million to complete an **environmental impact statement** for alternatives/improvements to the SR520 corridor;

- **Parks functional area expenditures** totaled \$301,000 compared to \$642,000 the same period last year. The higher expenditures in 2002 reflect installment payments for the Juel and NE Redmond Park properties. Significant projects in 2003 include installing a media lab and earthquake retrofitting for the Teen Center, both of which are nearly complete; award of bid with scheduled construction in the summer for Grasslawn Park Phase 2 improvements, and active construction of Perrigo Park.
- **Police functional area expenditures** were substantially the same as the previous year. Expenditures in the current biennium reflect security upgrades to the Public Safety Building.

Please refer to the attached appendix for further detail on CIP revenues and expenditures by functional area.

## CITYWIDE INVESTMENT REPORT

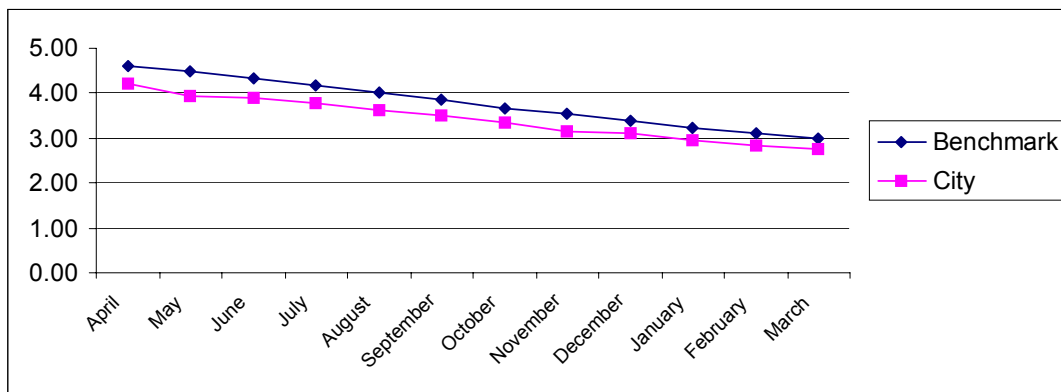
The city's investment portfolio continued to meet the primary objectives of the investment policy: safety of principal, liquidity of funds, and attaining a market rate of return given the risk constraints and diversification guidelines. The investment portfolio grew from \$108.8 million at the start of the year to \$114.9 million at the end of 1<sup>st</sup> quarter. Revenue receipts and investment interest continue to push cash balances higher.

The table below provides a snapshot of the city's portfolio and performance at March 31, 2003.

	<b>Book Value</b>	<b>Percentage of Portfolio</b>	<b>Days to Maturity</b>	<b>Yield To Maturity</b>
State Investment Pool	\$16,026,237	13.9%	1	1.30%
Certificates of Deposit	\$47,979,307	41.7%	209	2.91%
Federal Agency Issues	\$46,296,571	40.3%	668	3.07%
Federal Agency Discount Issues	\$2,278,186	2.0%	452	3.93%
Money Market Fund	\$2,369,644	2.1%	1	N/A
<b>Total Value</b>	<b>\$114,949,945</b>	<b>100.00%</b>	<b>366</b>	<b>3.11%</b>

The city currently benchmarks its portfolio to the 2-year average of the 2-year Treasury Note. The city earned an average interest rate of 2.85% during the 1<sup>st</sup> quarter versus the benchmark average of 3.11%. The city slightly under performed its benchmark for the 1<sup>st</sup> quarter of 2003 due to interest rates continuing to decline in response to concerns over the Iraq War and a sluggish economy. It is important to note that the benchmark return is based on a 2-year history of rates that includes, as part of its average, much higher levels than the current rates the city can obtain today. Over time the average of the benchmark will decline as the higher rates drop out of the equation, which will allow the city to once again meet or exceed its benchmark. The following chart compares the city's rate of return to the benchmark.

**Portfolio Benchmark Comparison**  
**April 2002 – March 2003**



# Appendix

## 2003 1<sup>st</sup> Quarter General Fund Revenues and Expenditures

<b>REVENUE COLLECTIONS</b>	<b>2003-04 Budget</b>	<b>2003 1Q Actual</b>	<b>% Received</b>	<b>2002 1Q Actual</b>
<b>Beginning Fund Balance</b>	\$ 0	\$ 5,037,773	0.0%	\$ 0
<b>Sales Taxes</b>	34,950,000	3,395,084	9.7%	3,474,141
Less Sales Tax on Construction	-2,200,000	-275,001	12.5%	-275,001
<b>Sales Tax - Criminal Justice</b>	1,940,000	224,640	11.6%	220,946
<b>Property Taxes</b>	20,076,000	80,679	0.4%	98,798
<b>Utility Taxes</b>				
Electricity	7,394,000	909,921	12.3%	852,391
Telephone	7,447,000	861,363	11.6%	760,530
Natural Gas	1,998,000	221,280	11.1%	335,157
Garbage Collection	921,000	106,439	11.6%	0
Cable Television	904,000	0	0.0%	98,004
Subtotal: Utility Taxes	18,664,000	2,099,004	11.2%	2,046,082
<b>Development Fees</b>	7,914,000	753,200	9.5%	1,359,982
<b>Intergovernmental</b>				
Fire & Emergency Services	9,286,000	0	0.0%	395,442
Overhead Fees	4,576,000	563,750	12.3%	546,176
Motor Vehicle Fuel Taxes	1,366,000	158,129	11.6%	156,460
Motor Vehicle Excise Taxes	0	0	0.0%	0
Liquor Profits & Taxes	812,000	134,390	16.6%	95,568
Federal/State/Local Grants	382,000	12,174	3.2%	12,417
Subtotal: Intergovernmental Revs	16,422,000	868,442	5.3%	1,206,063
<b>Other</b>				
Investment Interest	2,450,000	148,532	6.1%	345,463
Business Licenses	1,567,000	904,704	57.7%	708,635
Business License Penalties	60,000	358,824	598.0%	19,558
Admissions Tax	903,000	92,745	10.3%	64,078
Fines and Forfeitures	294,000	48,128	16.4%	60,726
Licenses and Permits	132,700	18,133	13.7%	19,073
Other	459,000	68,377	14.9%	174,418
Subtotal: Other Revenues	5,865,700	1,639,443	27.9%	1,391,951
<b>TOTAL OPERATING REVENUES</b>	<b>\$ 103,631,700</b>	<b>\$ 13,823,264</b>	<b>13.3%</b>	<b>\$ 9,522,962</b>

<b>DEPARTMENTAL EXPENDITURES</b>	<b>2003-04 Budget</b>	<b>2003 1Q Actual</b>	<b>% Spent</b>	<b>2002 1Q Actual</b>
Fire	\$ 21,177,047	\$ 2,458,518	11.6%	\$ 2,564,693
Police	19,819,528	2,205,352	11.1%	2,221,910
Non-Departmental	15,876,689	1,362,626	8.6%	1,480,726
Public Works	15,183,023	1,702,775	11.2%	1,920,530
Finance and IS	9,856,923	1,075,324	10.9%	1,181,233
Planning	9,290,503	1,125,220	12.1%	1,119,815
Parks & Recreation	8,254,954	865,593	10.5%	840,293
Human Resources	1,686,945	166,426	9.9%	137,402
Legal	1,200,031	110,381	9.2%	80,647
Executive	971,201	117,372	12.1%	91,225
Legislative	314,856	28,783	9.1%	24,241
<b>TOTAL EXPENDITURES</b>	<b>\$ 103,631,700</b>	<b>\$ 11,218,370</b>	<b>10.8%</b>	<b>\$ 11,662,715</b>



## 2003 1<sup>st</sup> Quarter Capital Investment Program Revenues and Expenditures

<b>REVENUE CATEGORIES</b>	<b>2003-04 Budget</b>	<b>2003 1Q Actual</b>	<b>% Received</b>	<b>2002 1Q Actual</b>
General Fund	\$ 5,389,195	\$ 684,207	13%	\$ 843,459
Real Estate Excise Tax (REET)	4,229,055	525,000	12%	575,000
Sales Tax on Construction	2,200,000	275,000	13%	275,000
Business Tax	12,761,116	3,922,372	31%	3,065,925
Impact Fees	5,191,000	1,240,543	24%	555,587
Private Contributions	405,280	292,574	72%	1,452,245
Federal/State Grants	5,880,126	0	0%	186,973
Investment Interest	2,528,003	462,386	18%	667,849
City Campus Project Revenue [1]	3,494,659	0	0%	0
Vehicle registration fees - local Option	800,000	9,992	1%	98,453
Half-cent motor vehicle fuel tax	624,000	73,936	12%	0
Other Revenue [2]	4,643,938	35,907	1%	44,068
<b>Major Revenue Source Subtotal</b>	<b>48,146,372</b>	<b>7,521,917</b>	<b>16%</b>	<b>7,764,559</b>
Beginning Fund Balance	46,499,575	0	0%	0
<b>TOTAL CIP REVENUES</b>	<b>\$ 94,645,947</b>	<b>\$ 7,521,917</b>	<b>8%</b>	<b>\$ 7,764,559</b>

[1] Reflect Utility and LID Guaranty Fund resources.

[2] Other revenue includes interfund transfers, intergovernmental revenue, and rental from parks houses.

<b>CIP FUNCTIONAL AREA EXPENDITURES</b>	<b>2003-04 Budget</b>	<b>2003 1Q Actual</b>	<b>% Spent</b>	<b>2002 1Q Actual</b>
Fire CIP	\$ 1,963,541	\$ 49,012	2.5%	\$ 64,019
Transportation CIP	43,514,643	1,029,001	2.4%	2,700,111
Parks CIP	18,274,705	300,803	1.6%	642,375
General Government CIP	15,031,448	12,290	0.1%	10,877
Police CIP	3,173,690	23,744	0.7%	5,100
<b>Total CIP Expenditures Subtotal</b>	<b>81,958,027</b>	<b>1,414,850</b>	<b>1.7%</b>	<b>3,422,482</b>
Ending Fund Balance	12,687,920			
<b>TOTAL CIP EXPENDITURES</b>	<b>\$ 94,645,947</b>			